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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

Ex Parte
CC Docket No. 94-1

April 30, 1996

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street - Room 222
Washington, DC 20554

Dear Mr. Caton:

On March 29, 1996, Whit Jordan, Maureen Keenan, Jeff Olson, Charles Cosson and Frank McKennedy, representing the United States Telephone Association (USTA), met with Les Selzer, Raj Kannan, Lori Huthoefer, Anthony Bush and Steve Spaeth of the Common Carrier Bureau Tariff Division.

The purpose of the meeting was to review with the Staff, USTA's proposal for a simplified total factor productivity calculation and other related issues in the Price Cap Review proceeding. Attached is the document provided to the Staff regarding these key USTA proposals.

An original and copy of this ex parte letter and attachment are being filed today due to intervening responsibilities.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Frank C. McKennedy", is written over a horizontal line.

Frank C. McKennedy
Director - Legal & Regulatory Affairs

cc w/o attachment: Les Selzer
Raj Kannan
Lori Huthoefer
Anthony Bush
Steve Spaeth

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LEC Price Cap Review**APR 30 1996****FEDERAL COMMUNICATIONS COMMISSION
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TFP is proper way to measure productivity.

- Christensen Simplified TFP method should be used by FCC to set X.
- All parties agree that LEC TFP growth averages about 2.7 to 3.1%.

USTA strongly supports a moving average X.

- Flows through gains.
- Facilitates removal of sharing, which should happen anyway.

No input inflation adjustment should be added to X.

- Inclusion would not change trend of price cap indexes.
- All tests show average "input inflation differential" is zero.
- Norsworthy tests the wrong question (the equality of the statistical distributions of annual growth rates, not the equality of the averages).
- The reason a statistical test for equivalence to zero is needed in the first place is the high degree of volatility caused by an "input price" adjustment term.
- No evidence of permanent shift at Divestiture.
- Measured differences are due to differences in measurement methods.

Should be no interstate adjustment to total TFP results.

- The existence of joint and common costs means that interstate TFP is not defined for telecommunications firms.
- Inputs and input growth cannot be meaningfully attributed to interstate only.
- Norsworthy's claim that assuming that interstate inputs grow at same rate as total is conservative is completely wrong. While such a measure cannot be made, if anything logics dictate that interstate inputs would have grown faster than intrastate, not slower as Norsworthy claims.
- The next unit of interstate output has the same productivity as the next unit of intrastate output.

CPD as an arbitrary addition to productivity must be eliminated

- The moving average aspect of USTA's plan ensures that any future increases in productivity are flowed through to customers.

Differences in Simplified Christensen TFP Approach from Original Christensen TFP Model

All data publicly available.

TFP calculation documented in single spreadsheet (TFP Review Plan).

All calculations displayed and all data sources documented.

Added Contel portion of GTE, Sprint (United, Centel), Lincoln.

Study begins in 1988, eliminating nonpublic USOAR adjustments.

Included results for 1994.

Output:

- **Booked intrastate long distance revenue -- rather than billed**
- **Booked intrastate access revenue -- rather than billed**

Labor:

- **Employees -- rather than weighted hours worked**

Capital:

- **Opportunity cost of capital measured for U.S. economy, using National Income and Product Accounts data -- rather than Moody' Public Utility Bond Yield data, measuring cost of debt only.**
- **U.S. Dept. of Commerce, Bureau of Economic Analysis (BEA) price indexes for capital prices -- rather than company proprietary Telephone Plant Indexes (TPIs).**
- **1988 beginning of year capital stock used for capital benchmarks calculated from public data -- rather than using company proprietary TPIs and other private data.**
- **Three-year moving average of cost of capital and capital gains in rental price equation.**
- **Simplified computation by consolidating those capital accounts that use the same economic depreciation rates and capital price indexes.**

Bottom Line: Results change very little from original study results.

Documentation of Simplified TFP Methods

USTA adopted the FCC's Tariff Review Plan standards for development of documentation.

USTA documented the effects of each of these changes on the results.

- **First, using the original data set filed by USTA in the first round of the LEC Price Cap Review (CC Docket No. 94-1, NPRM):**

USTA Comments, Attachment A, Tables 1 - 8

- **Second, using public data, the expanded set of 11 price cap LECs, with updated data through 1994:**

USTA Comments, Attachment A, Table 9; and Attachment B (Total Factor Productivity Review Plan)

This approach allows the Commission to examine the effects of each modification made by USTA.

USTA Has Responded to Requests for Data

Ad Hoc and AT&T have requested data from USTA.

- **USTA and AT&T have cooperated to ensure that requests are handled without wasting the Commission's time or resources.**

Ad Hoc Data Requests and Motions

- **It is clear from Ad Hoc's data requests and Motions that Ad Hoc has all of the information necessary to analyze and replicate USTA's productivity model.**
- **Ad Hoc continues to attempt to persuade the Commission through political tactics, not economic arguments.**

USTA has responded to all of the requests.